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DIRECTORATE OF INTELLIGENCE

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CHINA: QUARTERLY ECONOMIC REPORT

Third and Fourth Quarters, 1983: Budget Worries,
Another Record Grain Harvest

Summary

China's industry showed signs of slowing in the fourth quarter, after three quarters of accelerating growth. Low product quality was still a major problem, and the inability to cut manufacturing and operating costs was partly to blame for a larger than expected budget deficit. Grain production set a new record, contributing to another good year for agriculture. In foreign trade, import growth again reached double-digits; exports, too, made a good, but less spectacular recovery.

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Industry

Industrial growth continued to accelerate in Jul-Sept, reaching 12.7 percent before easing to 10.5 percent in the fourth quarter (see table). This was the pattern in both heavy and light industries.

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In heavy industry, where output had grown at a double-digit clip all year, the rate of increase rose to 13.6 percent in the third quarter and then slipped back to 10.0 percent in the final three months--the slowest quarterly growth since the final quarter of 1982. A fall-off in energy production contributed, directly and indirectly, to this fourth-quarter decline. Energy

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This memorandum was prepared by [redacted] with contributions by [redacted] of the China Division, Office of East Asian Analysis. Comments and questions are welcome and may be directed to the Chief, Domestic Policy Branch [redacted]

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output growth, which shot up to 7.3 percent in the third quarter, fell sharply to 2.6 percent in Oct-Dec. For the year, energy growth reached 5.0 percent. [redacted]

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Machinery and equipment industries were the strongest performers in the second half. Data for Jan-Nov show four major product lines with growth rates higher than heavy industry as a whole: power generating equipment (73.8 percent), mining equipment (48.5 percent), motor vehicles (23.7 percent), metal cutting machine tools (18.1 percent). **Building materials** industries continued their rapid expansion. Cement output grew by 12.6 percent in Jan-Nov and plate glass production by 15.1 percent. After midyear, when output was growing by 6.3 percent, chemical fertilizer production picked up, reaching 7.5 percent overall for Jan-Nov. [redacted]

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The improvement in **light industry** was striking; from 8.1 percent in the second quarter, the growth rate rose to 11.7 percent in Jul-Sept before dropping to 10.8 percent in the final three months. Despite tailing off, light industry accounted for 90 percent of the overall gain in industrial production in the fourth quarter (fourth quarter 1983 compared with third quarter 1983, unadjusted). [redacted]

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Consumer durables output posted large gains, ranging from 9.5 percent (in Jan-Nov) for watches to 46.6 percent for washing machines and 97.8 percent for refrigerators. Only sewing machines (down 14.4 percent) recorded less than strong growth. Although picking up in the third quarter, **textile and fibers** industries on the whole did relatively poorly in 1983. Synthetic fibers output grew by only 6.2 percent (Jan-Nov); cloth production dropped by 1.6 percent. [redacted]

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In its yearend press release, the State Statistical Bureau pointed out that "economic results were still not satisfactory." But the Bureau said that **quality and variety** had improved, and cited a survey of 75 products in which the quality of 64 showed some improvement or remained unchanged from 1982. This was better than in Jan-May, when the quality of 14 of the 75 commodities declined. Quality problems were especially serious among mechanical and electrical products. **Labor productivity** (gross output of state industrial enterprises divided by the number of workers and staff members) reportedly grew by 7.7 percent in 1983. The press release noted that **energy and industrial materials** were still in short supply and that **transportation** remained a bottleneck. [redacted]

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Beijing's obvious dissatisfaction with **economic results** can be explained in large part by the linkage between high costs and the shortfall in state budget revenues. For 1983 as a whole production costs fell by 0.2 percent, an improvement over Jan-Jun when costs actually rose by 1 percent. Budgetary projections, however, were based on a cost reduction of 1 to 2 percent; thus we believe Beijing was left with a budget deficit considerably

larger than planned. During the final quarter of 1983, the government put great pressure on enterprise managers to improve their profit positions, but there is no clear evidence that those efforts have had much of an impact on state revenues. [REDACTED]

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Agriculture

Preliminary data on agricultural performance indicate another good year despite serious flooding and less than ideal crop conditions in some areas. Beijing's preliminary estimate for grain output is 370 million tons, 4.7 percent above 1982's excellent harvest. Increases have also been announced for: cotton (11 percent), sugar (2.6 percent), meat (0.2 percent), milk (17.1 percent), eggs (16.1 percent), and aquatic products (2.8 percent). Edible oil production may have declined. Because state purchasing centers had difficulty purchasing and storing the greatly expanded supplies of edible oil that peasants offered for sale in 1981-82, the government has been trying to control production. [REDACTED]

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Foreign Trade

After a two-year decline, China's imports of capital equipment and industrial supplies began to pick up speed in mid-1983. While Beijing fell far short of the 40 percent increase planned for 1983, by yearend imports were running well ahead of 1982 levels. Total imports probably exceeded \$18 billion for the year, an increase of about 11 percent. Purchases of agricultural commodities fell for the first time in several years, due both to bumper crops at home and trade disputes with the United States. Chinese exports, on the other hand, continued to encounter problems in the developed West where recession and growing protectionism hampered growth. Most of the estimated 2.1 percent increase, to \$24 billion, came in the second half as a result of increased sales to the USSR, Eastern Europe, and the Middle East. Beijing's foreign exchange reserves continued to increase, probably surpassing \$15 billion, up almost \$4 billion from the end of 1982. [REDACTED]

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China's purchases from the US amounted to \$2.2 billion in 1983, compared with \$2.9 billion in 1982. Exports to the US totaled \$2.2 billion, down only slightly from 1982. [REDACTED]

Elsewhere in the Economy

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Retail Sales: The growth rate for consumer purchases fell in both September and October, the most recent months for which data are available. Still, the increase was 10.2 percent for Jan-Oct and probably held at around 10 percent for the year as a whole. Sales of durables, especially TVs, continued to make large gains. [REDACTED]

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Investment: Beijing's attempts to curb investment spending and to direct money and materials to key projects may be beginning to take hold. Capital construction grew by 11.3 percent in Jan-Oct, significantly below its 17.0 percent rate for Jan-Jun. Also, practically all of this increase was financed by funds from the central budget--state investment was up 18.3 percent. Self-financed investment by localities and enterprises showed only a 0.7 percent increase during Jan-Oct. This is in marked contrast to previous years when rapidly growing local investment siphoned building materials away from higher priority state projects. Assuming the normal yearend flurry of spending on capital construction and a rate of growth of 20 percent or so in spending on plant and equipment upgrading, total investment may have risen by 15 to 20 percent in 1983. All of the reported 11.3 percent increase in capital construction came in "productive" facilities (versus "nonproductive" housing, hospitals, schools). **Housing** investment was 10 percent below last year's, and the completion rate for housing under construction was down 14 percent. Data for Jan-Nov show that major spending increases came in energy (35 percent) and transportation (45 percent), areas in which the state plan called for major increases. [REDACTED]

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Transport: Rail transport, which ran above-plan in Jan-Jun when it was 3.8 percent over 1982, picked up in the third and fourth quarters. Growth in Jan-Sept was 4.1 percent and rose further in October to 5.2 percent. For Jan-Oct the rate was 4.2 percent. **Shipping**, which had shown signs of weakness, continued to falter in the third quarter. Growth fell from 2.2 percent in Jan-Jun to 1.1 percent for Jan-Sept, before rebounding in October and boosting the rate for Jan-Oct to 1.9 percent. [REDACTED]

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Outlook

We may see a slowdown in industrial growth during the next few months. In early October, spokesmen for the State Economic Commission (SEC) warned that unless managers cut back on production, inventories of fuel, raw materials, and semifinished goods would soon reach dangerously low levels. Since expansion continued essentially unchecked in Oct-Dec, it is likely that inventories are now below normal and that managers are finding it increasingly difficult to sustain current production rates. [REDACTED]

There are other reasons to expect a slower pace of growth. Beijing appears to be losing its patience with managers who continue to neglect product quality and costs. The announcement by the head of the SEC that quality and variety goals are to be included in the annual economic plan suggests that Beijing is now ready to take firm measures to deal with these persistent problems. Implementation of new standards may cause some reduction in growth while quality control and cost reduction measures are sorted out. Finally, to the extent that efforts to control investment have begun to take hold, the rate of industrial growth will decline. With a slowdown in industry, of

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course, gains in wages, in retail sales and in employment would tend to be smaller; and inflationary pressures would ease. [REDACTED]

At this stage, prospects for other sectors look good. In agriculture, the winter wheat crop has done well, and we anticipate a good, perhaps even record, harvest. In foreign trade, we expect exports to remain on a slow upward trend during the next several months; imports--led by industrial raw materials and capital goods--are likely to continue to exhibit the rapid gains that we saw in late 1983, when growth once again broke into the double-digit range. [REDACTED]

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	Quarters					Annual		
	1982	1983				1981	1982	1983
	IV	I	II	III	IV Preliminary			Preliminary
<u>International Trade and Finance</u>	(Million \$US, except where noted; percent change from previous year in parentheses)							
Total Exports (fob)	6063.9 (1.7)	5665.2 (-0.9)	5758.8 (0.5)	6247.6 (4.3)	6300. (3.8)	21,495.5 (13.9)	23,502.4 (9.3)	24,000 (2.1)
Total Imports (fob)	4181.0 (-1.5)	4069.5 (-3.4)	4500.6 (5.3)	4439.9 (12.2)	5000 (19.6)	17,948.9 (-6.4)	16,625.0 (-7.4)	18,000 (8.3)
Trade Balance	1882.9	1595.6	1258.2	1807.7	1300	3546.6	6877.3	6000
Oil and Petroleum Product Exports	1263.2 (-2.0)	1100.2 (-8.1)	991.7 (-4.1)	NA	NA	4594.5 (10.3)	4784.1 (4.1)	NA
Grain Imports (Thousand tons)	3656 (8.9)	4643 (44.7)	3553 (-14.7)	2198 (-44.4)	2500 (-31.6)	13,204 (-3.4)	14,984 (13.5)	12,900 (-13.9)
Foreign Exchange Reserves	11,125 (133.1)	12,408 (138.4)	13,022 (84.5)	14,066 (52.4)	15,000 (34.8)	4773 (111.0)	11,125 (133.1)	15,000 (34.8)
Exchange Rate (avg. yuan/dollar)	1.9722	1.9528	1.9873	1.9837	1.98	1.705	1.889	1.980
<u>US-China Trade</u>								
Exports to US	540.2 (11.6)	534.9 (-3.4)	536.0 (10.0)	611.2 (-11.9)	562.0 (4.0)	1874.9 (77.1)	2274.9 (21.3)	2245 (-1.3)
Imports from US	518.5 (-43.8)	668.8 (26.1)	365.2 (-54.5)	397.8 (-42.1)	738.0 (42.3)	3602.7 (-4.1)	2912.0 (-19.2)	2170 (-25.5)
Trade Balance with US	21.7	-133.9	170.8	213.4	-176.0	-1727.8	-637.1	74
<u>Japan-China Trade</u>								
Exports to Japan	1282.7 (-14.0)	1145.0 (-11.9)	1148.9 (-8.1)	1265.3 (1.2)	1270 (-1.0)	5031.8 (21.6)	5083.4 (1.0)	4830 (-5.0)
Imports from Japan	923.5 (-19.5)	871.0 (2.6)	1232.0 (38.7)	1278.3 (52.2)	1530 (65.7)	5076.0 (-0.6)	3500.0 (-31.0)	4910 (40.3)
Trade Balance with Japan	359.2	274.0	-83.1	-13.0	-260	-44.2	1583.4	-80

China: Selected Economic Indicators

	Quarters					Annual		
	1982	1983				1982	1983	
	IV	I	II	III	IV Preliminary	Actual	Chinese Plan	Preliminary
Production (Bil 1980 Yuan, except where noted otherwise; numbers in parentheses are percent change from previous year)								
Total Industry	148.71 (4.1)	138.29 (7.1)	158.61 (10.3)	153.53 (12.7)	164.27 (10.5)	557.9 (7.7)	580.2 (4.0)	614.7 (10.2)
Heavy Industry	72.73 (7.9)	69.33 (11.7)	81.27 (12.7)	78.96 (13.6)	80.04 (10.0)	276.4 (9.9)	287.2 (3.9)	309.6 (12.1)
Light Industry	75.98 (1.6)	68.96 (2.5)	77.34 (8.1)	74.57 (11.7)	84.23 (10.8)	281.5 (5.7)	293.0 (4.1)	305.1 (8.4)
Agricultural Production						256.6 (11.0)	266.9 (4.0)	NA
Grain Production (Million tons)						353.4 (8.7)	NA	370.0 (4.7)
Energy Production (Million tons coal equivalent)	181.14 (-5.2)	162.19 (5.2)	176.81 (5.2)	176.71 (7.3)	185.78 (2.6)	668.0 (5.7)		701.5 (5.0)
Oil Production (Million tons)	25.28 (-0.9)	25.88 (2.1)	26.33 (1.0)	26.65 (4.7)	27.12 (7.3)	102.1 (0.9)	100.0	105.99 (3.8)
Aggregate Indicators						1981 993	1982 1008	
Population (Mil on July 1)						(1.2)	(1.5)	
Gross National Product (Bil 1982 \$US)						280 (3.0)	300.7 (7.4)	
GNP per capita (1982 \$US)						282 (1.8)	298.3 (5.8)	
State Budget (Bil yuan)								
Revenues						109.0 (0.5)	110.7 (1.6)	
Expenditures						111.5 (-8.1)	113.7 (2.0)	
Deficit (-) or Surplus (+)						-2.5	-3.0	

SUBJECT: China: Quarterly Economic Report

EA M 84-10024

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